



AMWH Portfolios

In the first two quarters, the Global Equity portfolio (GES) returned 10.4% and the Energy Transition strategy (ET) returned 18.2%. Please see our fact sheets for more details (pages 8-11).

Market Overview

It would have been a bold prediction to forecast financial markets ending the second quarter where they started before Liberation Day. Markets swooned after tariffs were announced. But by the end of the quarter, US equity markets were making new all-time highs (driven by a small cohort of big tech stocks), corporate bond spreads were near all-time lows, equity and bond implied volatilities were low, inflation expectations were falling, and US Treasury yields were falling all across the yield curve.

Recent history is well known. "Liberation Day" imposed steep tariffs globally on US imports, only for these to be temporarily paused as US Treasury bond markets displayed stress. The hot Israel/Iran war broke out, with hostilities ending only with direct US military intervention. In the US, the Big Beautiful Bill was narrowly approved. President Trump raised his pressure on the independence of the Fed, calling for lower interest rates and mulling announcing his candidate for chair well before Mr. Powell's term ends next year.

These were only the main events. The consequences of each remain to be seen. Only three of the promised ninety tariff deals were concluded by the July 9th deadline, and the process has now started again with the imposition of higher tariff rates. The economic and financial consequences of tariffs will play out only over time. It would be foolish to imagine that Iran's nuclear ambitions have been permanently quashed. They have certainly been delayed, but the resolve to follow a North Korean course is now much more likely. The BBB has significant implications for government finances which will become apparent only over time. Pressure to lower interest rates to reduce the government interest rate burden, while the Fed is concerned about the inflationary consequences of tariffs and tighter labor markets, is an uncomfortable combination.

Ascribing a narrative to market action is usually unwise in our experience, but the view that, while professional investors are cautious, retail investors have bought the dip may have some truth to it. Financial markets appeared to be signaling that all is well. Yet there is controversy. Economists warn of the inflationary consequences of tariffs and lax fiscal policy. Equity investors appear to believe that either tariffs don't matter or that they will be low



enough not to matter, that real assets (equities) are adequate protection from inflation, and that lower interest rates, tax cuts and deregulation will cause a following wind.

Despite hostilities in the Middle East, gold paused its long ascent. Because of hostilities in the Middle East, the price of oil stopped falling. The Fed held interest rates, citing decent economic growth, low unemployment, sticky inflation, and the need to see the impact of tariffs on prices. But perhaps the most important clue was the weakness of the US\$, in spite of high interest rate differentials in its favor. It has fallen through the bottom of its trading range for the last three years. Investors may not be selling US financial assets yet, but they are almost certainly hedging their currency risk. The issue of trust in the US cannot be dismissed. A weaker US currency and the burden of tariffs adds to inflation pressures. It's a challenging time for investors.

Investment Returns

At the index level, the concentration and strength of technology stocks was notable. Over half of S&P 500 gains in the quarter were generated by three stocks, NVDA, MSFT and AVGO¹.

Global Equity (GES)

In the quarter, the portfolio rose in value but underperformed the S&P500 and the ACWI indices. It has gained in value, outperforming both indices on a year-to-date basis.

Stock picking aided GES, despite the underweight to Tech and cash drag. Stock selection contributed strongly. Traditional energy was the primary laggard, although it was notably volatile through the quarter (particularly during the escalation of the Iran conflict).

Attribution by Sector - GES

- Industrials were again the largest sector contributor to performance. It is the portfolio's largest GICS allocation
- The relative underweight to Tech was a drag; -2% of allocation and -1% of security selection effect
- Stock picking remains a highlight and helped mitigate some of the portfolio's UW to tech (2.4% of positive stock selection effect)
- Non-USD bias was positive, adding 62bps of return

¹ S&P 500 Attribution: NVDA 2.6%, MSFT 2.0%, AVGO, 1.1% - Source: Bloomberg



Attribution by Holding - GES

- Returns were broadly based, with 18 names adding more than 20bps in the quarter
- Traditional energy was a portfolio laggard with CVX costing 42 bps, OIH 19bps, XOM 13bps
- Only 3 names cost more than 20bps (CVX, BRK/B, AES)

Energy Transition (ET)

In the quarter, the portfolio gained in value, outperforming both the S&P 500 and ACWI indices. It has gained in value year to date, also outperforming both indices.

- The concentrated energy portfolio had 7.5% of positive stock selection effect, outweighing the lack of tech exposure vs. broad market indices
- Returns were concentrated, and nuclear and carbon capture names led the way
- AEP and AES were the largest detractors
- Traditional energy was the worst-performing S&P 500 sector (ET holdings slightly outperformed)

Investment Outlook

Our previous letters have discussed the structural, secular and intergenerational changes that we try to position the portfolios to benefit from. None of this thinking has changed. This quarter, it is necessary to assess how we should navigate the prevailing fluid policy environment. The US administration is attempting to swing for the fences in stimulating economic growth, while restricting trade and rebuilding a broader US industrial base. Simultaneously, huge AI related capital spending is highlighting physical constraints in electricity reliability and supply. Water availability is becoming an issue, too. Is policy coherent, and if not, what are the inconsistencies that we should be alert to?

Who pays tariffs? Realistically, the cost of tariffs will be shared all through the supply chain from producer to consumer. We don't know exactly how yet, and the way the burden is shared will vary from category to category. The Fed's caution in waiting to assess the impact on consumer prices is justified. But equity investors should be equally cautious, and assess the effects on company margins and profits which are where the burden of sharing the costs of tariffs will be partly felt. Inventories were built up in advance of the imposition of tariffs (the US reported its largest ever trade deficit, and China has just reported its largest ever trade surplus). Impacts on prices, margins and profits will only become apparent gradually over the rest of the year.



If we're wrong about burden sharing, and tariffs are passed on to end consumers, inflation will be higher. If tariffs aren't passed on to consumers, margins and profits will be squeezed more. Neither of these are attractive scenarios for investors. We rely more on the caution of company managements in making their plans for the new business environment as a guide to portfolio investment choices. Equity markets don't yet appear to be discounting this.

In the US, the administration is asking investors to believe that accelerating economic growth and tariff receipts will fund the combination of tax cuts and a large net increase in government spending set out in the BBB. Maybe the Laffer Curve will work, although it hasn't since the theory was first introduced in the Reagan administration. Leaving this aside, it is worthwhile to look at the scale of the fiscal challenge. The extension of President Trump's 2017 tax cuts was expected. Additional cuts of about \$160 billion (overtime, tips, car loans) were surprising, as was increased spending on defense and border security of about \$280 billion. Much of the fiscal impact is designed to be felt during the current administration in the drive for growth.

US fiscal policy has been manageable through the financial crisis, QE and Covid in the sense that the Treasury bond market hasn't revolted. But it must be noted that the BBB raises government debt interest costs to about 25% of total revenue. It's a valid question as to whether this is sustainable. The test will be the evolution of inflation both as a result of deficit spending and tariff pressures on consumer prices. Attempts by the administration to push down interest rates won't improve investor confidence. Reduced Federal spending in the US will also have the corollary of higher State spending, as States have to take up more of the responsibility for essential social programs such as healthcare and disaster relief. State tax rates are very likely to rise, and whatever the claims of the BBB, the overall tax result for US persons may well be unfavorable.

We should note that the US is not alone. Rising fiscal deficits and slowing economic growth are big issues in, amongst others, Germany, France, the UK, Spain, Holland, India and, perhaps most importantly, China. Tariffs and increased defense spending are adding to fiscal problems in the developed countries. The point is that rising fiscal deficits are a global challenge. What are the chances that an inward-looking, mercantilist approach can work for any individual country? We can't yet answer the question, but we must be conscious of it.



All of this must be set against the starting point today in financial markets. At the end of the second quarter US equity markets were making new all-time highs (driven by a small cohort of big tech stocks), corporate bond spreads were near all-time lows, equity and bond implied volatilities were low, inflation expectations were falling, and US Treasury yields were falling all across the yield curve. Equity valuations were expensive compared to history. Investment returns have been good so far this year. Investment in the physical bottlenecks in the global economy has been rewarded. But it seems to us that current market levels, policies that stimulate geopolitical competition, and increasing fiscal problems create an unfavorable asymmetry. Portfolios should be structured to be very different from the market.

Our final point is about long term change. We believe that the global economic and financial system can be seen as a series of very long cycles. Each cycle is characterized by a generally accepted consensus. Each cycle reaches an end when distortions become too great to allow the consensus to continue.

For example, the cycle that began at the end of WW2 was about reconstruction, jobs for the returning soldiers, and the state as the source and allocator of capital. It failed in the late 1970s, when labor and unions became too powerful, inflation rose to very high levels, and state finances deteriorated. The next cycle that began around 1980 was based on the desire of the baby boom generation to consume and lower taxes, and reliance on the private sector to provide and allocate capital. This cycle is ending because the preoccupations of the baby boomers (retirement, health) are an extreme burden on the economy, population growth is slowing or negative, the intergenerational investments of the post WW2 cycle (public goods, infrastructure) have been fully amortized and arguably have not been replaced, and fiscal deficits are expanding in an effort to keep the old cycle going.

We think the current political environment reflects these transitional stresses. But we do not think there is yet a clear picture of what consensus replaces the old baby boomer centric view. For example, the needs and aspirations of younger generations are not central to policy. Private capital, with the exception of technology, has become more and more short term in focus. But there is evidence emerging of fresh intergenerational investment, of which the energy transition, notably in the grid and in reliable baseload, is a good example. And AI may be part, but will not be all, of the solution.



A long cycle transition is therefore under way, but the politics of the moment will be controversial until a new consensus emerges. In the meantime we are wary of the investment challenges posed by an analysis based on the consensus of the past.

Portfolio Positioning

Despite the cascade of global events and fluctuating policy developments in the US, portfolio strategy, which concentrates on the medium and longer terms, has not changed. Headlines and news flow as political tools only mask the structural and secular factors which define our investment strategy.

The main allocations of capital in our Global portfolios are set out below. Energy Transition portfolios are a subset.

1. We're still wary of starting aggregate valuations for equities in the US. We think that global frictions in the form of retooling supply chains, tariffs and growing national and regional competition will become headwinds to company returns.
2. We don't assume liquidity in financial markets, nor do we believe that we can time when our investment ideas work. We prefer to position portfolios when we can, rather than when circumstances dictate. We avoid illiquid investments. Circumstances when liquidity might be worth a significant premium now seem likely.
3. We are wary of the weight and concentration of AI investments in equity indices. We prefer in our portfolios to make careful individual stock choices, and to have much lower aggregate exposure in our portfolios than in equity indices. This is a somewhat contrarian view, which allows us to diversify portfolios better.
4. We believe we are in a world of digital abundance and physical scarcity. This supports the case for proportionately much greater exposure to energy in portfolios than is present in equity markets. The tech companies' continuing scramble for available, reliable power (and water) supports the notion of a bottleneck. Our logic is that these investments should be at least the same weight in portfolios as exposure to technology. Under the general heading of energy, we're careful to avoid categories where capital has been overallocated, and instead to focus on areas where capital is scarce. Our working assumption is that long-term energy supply will be a mix of hydrocarbons, nuclear and alternatives. For alternatives, the prerequisite is distribution and storage infrastructure that is so far lacking. Although the energy complex is caught up in fears for economic growth, we think the medium term case is strong, as an essential prerequisite for a successful economy.



5. We're wary of the degree of leverage supported by the economy. To us, at least, private credit is opaque, and probably provides better returns for its intermediaries than for end investors. It's definitely illiquid. We avoid credit risk and leveraged balance sheets in portfolios. Recent adverse developments in rates and credit markets support this view.
6. We have some exposure to undervalued pharmaceutical company R&D. This is largely uncorrelated to global political and financial headwinds, and in the meantime these companies pay attractive dividends. Healthcare spending accounts for about 17% of GDP in the US, almost double European levels. We avoid the complex chain of intermediaries in the US system that are likely to come under political pressure in the search for lower healthcare costs, and in the tariff agenda.
7. We maintain holdings in gold bullion while the possibility of more extreme financial or geopolitical discontinuity exists. We view this position as an insurance policy that would be valuable in times of distress.
8. For similar reasons we hold a significant position in cash (see fact sheets for allocations). Interest rates make this decision easier. The value of cash will be realized if and when we can act in times of significant market distress.

Please get in touch if you have any questions or if you would like to join the investment conversation. All ideas are welcome!

Sincerely,

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